SUPREME COURT, U. S.

FILED

FEB 23 1976

MICHAEL RODAK, JR., CLERK

In The

SUPREME COURT OF THE UNITED STATES

January Term 1976

NO. 75-1204

GENE GALL, and CECILE FLORENCE GALL,

Petitioners

v.

UNITED STATES OF AMERICA,

Respondent

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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In The

SUPREME COURT OF THE UNITED STATES

January Term 1976

No.....

IN THE MATTER OF: GENE GALL, and
CECILE FLORENCE GALL,

Petitioners

v.

UNITED STATES OF AMERICA,

Respondent

PETITION FOR A WRIT OF CERTIORARI TO
THE UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

The Petitioner prays that a Writ of Certiorari issue to review the judgment and opinion of the United States Court of Appeals for the Fifth Circuit entered in the above case on October 23, 1975.

JURISDICTION

The Judgment of the Court of Appeals was entered October 23, 1975. The Petition for Rehearing was denied November 28, 1975. This Petition for Certiorari is filed within ninety days of that date. The jurisdiction of this Court is involved under 28 USCA Section 1254(1).

OPINION BELOW

The judgment of the United States District Judge was entered April 7, 1975.

The Petitioner timely appealed to the United States Court of Appeals for the Fifth Circuit which affirmed the judgment of the District Judge on the 23rd day of October 1975.

The Petitioner filed Motion for Rehearing In Banc which was overruled on November 28, 1975.

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QUESTION PRESENTED

Whether the gifts by Petitioners to trusts for their two daughters during the years in question qualify for the donor annual exclusion provided for in the Internal Revenue Code of 1954, Section 2503 (26 U.S.C.).

NOTE

The United States Court of Appeals for the Fifth Circuit will be referred to as Appeals Court. The United States District Court for the Northern District of Texas and the Judge thereof will be referred to as District Court or District Judge. Appendix will be shown in Index and will be referred to as "A".

STATEMENT OF THE CASE

This is a suit to recover gift tax paid by Petitioners. In 1960, Petitioners created four trusts; being two trusts each for the benefit of each of their daughters, Denise Ann Gall, born Febru-

ary 16, 1955 and Terry Lynne Gall, born May 16, 1956. Two of such trusts were identical except that one was for each of their two daughters. These trusts did not qualify for the $3,000 annual gift tax exemption as allowed by 2503 Internal Revenue Code. They did qualify for the $30,000 lifetime exemptions. These trusts are not in controversy.

The other two trusts created by the Petitioners were identical to each other but different from the two trusts not in controversy. These trusts were created, one for each of Petioners' daughters (known as 21 year trusts) and it is the gifts to these trusts to which Petitioners claimed the $3,000 annual exclusion as allowed by 2503 Internal Revenue Code. These are the two trusts that are now in controversy.

The Republic National Bank of Dallas was Trustee for each trust under

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a written trust agreement executed by Petitioners and said bank.

The trusts qualify in every respect except that part thereof in controversy which reads as follows:

"(4) Should TERRY die before attaining the age of twenty-one (21) years (or the age of 30 years, if this trust is extended pursuant to the provisions of subparagraph (3) of this paragraph), this trust shall terminate, and the entire trust property then remaining shall be paid over and distributed to such persons, in such shares, and in such manner as TERRY may appoint by her last will, duly admitted to probate by a Court of competent jurisdiction, provided this power of appointment is specifically referred to by the terms of such will; and provided, further, that this power of appointment can be

exercised by TERRY only in the event that she is over the age of nineteen (19) years at the time of executing such will.

(5) Should TERRY die before attaining the age of twenty-one (21) years (or the age of 30 years, if this trust is extended pursuant to the provisions of subparagraph (3) of this paragraph), and without validly exercising the general testamentary power of appointment referred to in subparagraph (4) of this paragraph, the Trustee shall pay over and distribute the entire trust property then remaining to the then surviving issue of the Grantors in equal shares per stirpes, or if there be no such issue of the Grantors then surviving, to the person or persons who shall be appointed to administer the estate of TERRY to be disposed of as a part of

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such estate.

During the years 1960, 1962, 1963, 1964, 1965 and 1966, Petitioners made gifts to these trusts and took the $3,000 annual exclusion in each trust. The Internal Revenue Service denied such exclusions and assessed additional tax against Petitioners in the amount of $8,097.12. This amount was paid on November 25, 1972. Timely application for refund was made and disallowed. Petitioners filed suit in the United States District Court for the Northern District of Texas seeking a recovery of such amount plus interest. The case was heard by the District Judge, without a jury, upon the pleadings, stipulations and evidence. The District Court denied recovery on April 7, 1975.

Appeal was taken to the United States Court of Appeals for the Fifth

Circuit which denied an appeal.

The United States District Judge states in his Memorandum Opinion: "At trial the Plaintiffs introduced evidence that they had fully intended to meet the requirements of Section 2503 when they executed the trusts. A reading of the instruments certainly gives that impression...".

Article 57 of the Texas Probate Code, as it existed in 1960, reads as follows:

> "Who May Execute a Will - Every person who has attained the age of nineteen years, or who is or has been lawfully married, or who is a member of the armed forces of the United States or of the auxiliaries thereof or of the maritime service at the time the will is made, being of sound mind,

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shall have the right and power to make a last will and testament, under the rules and limitations prescribed by law. Acts 1955, 54th Leg., p.88, Ch. 55)."

At the trial, Petitioners testified that they consulted the bank and stated their desire to have trusts that would qualify for the annual exclusion. Counsel drawing the instruments testified he was employed by the bank to write the trust instruments, that he was familiar with Article 57 of the Texas Probate Code but inadvertently failed to include the exceptions stated in Article 57.

REASONS FOR GRANTING WRIT

Implicit to a consideration of the question presented are the following:

Were the restrictions in the trust of the substance so as to deny Petitioners refund of taxes?

Whether Petitioners, because of an inadvertent omission by the draftsman of the trust should be denied a refund;

Whether Article 57 of the Texas Probate Code may be read into such trusts;

Whether the restriction in Regulation 2503-4 is invalid;

Whether the intent as shown by the instruments themselves and the evidence should be considered; and

Whether the fact that at the time of the assessment the beneficiaries of such trusts were under fourteen (14) years of age and at the time of trial were unmarried and over nineteen (19) years of age should be considered.

This is a case of most importance. No case has been found that directly passes upon the proceedings, stipulations and evidence of this case. In the case of Harris v. Commissioner (5th) 461 F.2d

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139, the Court of Appeals discusses unsworn testimony as being insufficient. Article 2503(c) Internal Revenue Code does not speak of restrictions being a matter of substance. This is found in the Regulation 25:2503-4(b). This restriction is invalid as it places a heavier burden on Petitioners than contained in 2503(c) Internal Revenue Code. The Code states that the trust passes to the donee on his attaining the age of twenty-one (21) years and in case of death, to the estate of the donee or as he may appoint under a general power of appointment as defined in 2514(c) I.T.C. The power of appointment exercised in the trusts qualify as a general power of appointment under 2514(c) and also qualify under 2503(b). 2514(c) reads as follows:

"For the purposes of this section,

> the term 'general power of appointment' means a power which is exercisable in favor of the individual possessing the power (hereafter in this subsection referred to as the 'possessor'), his estate, his creditors, or the creditors of his estate;".

The District Court and the Court of Appeals do not object to the trusts except that portion that provides that the minor must be nineteen (19) years of age to appoint by will and that such term is more burdensome than the Texas statute. If the drafter of the trust had stated except as otherwise provided in Article 57 of the Texas Probate Code, the minor must be 19 years of age to exercise his power of appointment under a will or if the last sentence of paragraph 4 of each trust "that this power of appointment can be exercised by donee

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only in the event that she is over the age of 19 years at the time of executing such will" were eliminated, there would have been no contest of such trust as that would have met all requirements of Section 2503 of the Code. The Courts in their separate opinions state that the failure to include such provisions is fatal because the donee may have married before she was 19 years of age. This is not so.

The question of whether the trusts created a present or a future interest is determined by the facts and circumstances of each case. The judgment of the District Court and Court of Appeals is in conflict with Josephine F. Rollmon v. U. S. (United States Court of Claims) 342 F.2d 62. Gilmore v. Commissioner of Internal Revenue (6th) 213 F.2d 520. Williams v. U. S. (United States Court of Claims) 378 F.2d 693 and Kieckhefer

v. Commissioner of Internal Revenue (7th) 189 F.2d 118.

In the Gilmore case, it is stated that "future interests" means an interest limited to commerce in use, possession or enjoyment at some future date, quoting U.S. v. Pelzer 312 U.S. 399. "An interest in property is a present interest if the donee has the right presently to use, possess or enjoy it" citing Fondren v. Commissioner 324 U.S. 18. The restrictions in the trusts are not such as to deny the exclusions. See also Doyle v. U.S. (2nd) 348 F.2d 715.

At the time of the assessment the beneficiaries were under 14 years of age, and could not marry under Texas law; and at the time of the trial, they were unmarried and over the age of 19. The questioned provisions in the trusts were of no force and effect. Since the

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power of appointment was a general power of appointment, it qualified under the provisions of 2503. Power of appointment is general if no restrictions were imposed upon the donee as to the person or persons whom he may appoint and the sums he may receive. If the donee had married before reaching the age of 19 years and made a will and died before she was 19 years of age, the will would have been perfectly valid for two reasons. (1) Article 57 of the Texas Probate Code, as it existed in 1960, is a general law and states the public policy of the State of Texas so that such provisions would have been invalid or the provisions of Article 57 would have been read into the trusts. (2) A trust instrument is a contract between the donors and the bank. Article 7425b-3 of the Texas Trust Act Laws in existence at the time and place of making of a

contract as well as laws then existing at the place where the agreement is to be performed constitute an integral part of the contract as if they had been expressly incorporated therein. The expressions contained in Article 57 can be read into such trust so that they will conform to such Article.

Winder Bros. vs. Sterling (Commission of Appeals of Texas, adopted by Supreme Court), 12, S.W. 2d 127; Longever vs. Miller (Sup. Ct.), 76 S.W.2d 1025; Globe Indemnity Co. vs. Barnes (Commission of Appeals). 288 S.W. 121; Poye v. State, 230 S.W. 161; Chesser v.Murphy, 386 S.W.2d 164; Great American Reserve Insurance v. Laney, 488 S.W.2d 481; Reid v. Gulf Oil,323 S.W.2d 107, aff. 337 S.W.2d 267.

Laws in force at time and place of making contract form a part of it as if

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they were expressly incorporated in its terms. East Texas Motor Freight vs. United States, 239 F.2d 417. Judge Cameron of the Fifth Circuit says:

> "Laws in force at the time and place of making of a contract enter into and form a part of it as if they were expressly incorporated in its terms".

The contract and statutes are construed together. Empire vs. State (Sup. Ct.), 47 S.W.2d 265.

Parties by agreement cannot repeal or modify a statute. Housing Authority vs. Lira, 282 S.W.2d 746; Empire vs. State, 47 S.W.2d 265; Texas Pacific Oil Co. vs. Stuard (e.r.), 7 S.W. 2d 878, see also Chesser v. Murphy and Great American Reserve Insurance cited above.

The opinions of the District Judge and the Court of Appeals are in

direct conflict with the laws with the decisions above referred to. The contract and statute are construed together. Parties by agreement cannot repeal or modify a statute. The time of making the trusts in question was 1960; the place was Dallas, Texas; the performance was by the Republic National Bank of Dallas, the Trustee. The property conveyed by the grantors to the Trustee was personal property, and the laws of Texas control.

In 17 A.J., Sec. 257, p.654, it is stated that all existing laws relating to the contract are made a part of it and must be read into it just as if the express provision were inserted in the contract at the time and place of making of the contract. This trust agreement is governed by the laws in existence at the time it was made. The above statements are sustained by the Federal Courts

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and most of the states, including Texas. Since Article 57 of the Probate Code of Texas is implied and read into each of such trusts, the fact that the exceptions were omitted is of no importance because the law itself is an integral part of the trust agreements. The execution of such trusts was a contract between the Petitioners and the bank. The bank undertook to operate the trust in accordance with its terms for a valuable consideration. Article 7525b-3 of the Texas Trust Act says such trusts may be created "to the same extent that he has capacity to make a contract."

It is clear, and the holding of the United States District Judge would seem to agree, that it was the intent of the Petitioners, the drafter and the bank to create such trusts that would qualify for the annual exclusion and that the draftsman inadvertently failed

to include the exclusions in Article 57 of the Texas Probate Code. Under such circumstances, it would appear that the Petitioners would not be penalized for his inadvertent error. It has been held that the intent in making these trusts is not conclusive but should be given more weight. U. S. vs. Williams, 395 F.2d 508 (5th).

In Krausse v. Barton, 430 S.W.2d 44, it is stated that in a construction to be placed on language used in a will, the language used in a will and the circumstances surrounding its execution must be considered. The District Judge says "a reading of the instrument certainly gives the impression" that they fully intended to meet the requirements of Sec. 2503 when they executed the trusts.

Under Texas law, it is held that in construing a trust the court's major

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task is to ascertain donor's intent with the view of effectuating it. Coffee vs. William Marsh Rice University, 408 S.W. 2d 269 (e.r.)

Taking the four corners of these trusts it was the intention of Petitioners to make such gift. In addition to the testimony of Petitioners, there was also the testimony of the counsel who drew such trusts of his intention to write the trusts so as to meet the exclusions and his inadvertence to include the exceptions in Article 57 of the Texas Probate Code.

The law on construction of wills applies to trusts. Intent is a factor. (See Williams case above), and Ralph S. Rice in Family Tax Planning referring to Article 2503 says: "The regulation states that the governing instrument can designate how the property shall be

distributed if the donee does and does not appoint. It cannot override any appointment donee makes, but this does seem to eliminate completely the statutory requirement that the property must go either into the estate of donee or as he appoints".

Petitioners urged the Court of Appeals to permit the amendment of such trusts under the facts and circumstances and so justice may be done to include the exceptions set out in Article 57 of the Texas Probate Code and would urge this court to do likewise.

CONCLUSION

For the foregoing reasons it is respectfully submitted that this Petition for a Writ of Certiorari should be granted.

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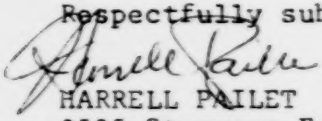
Respectfully submitted,



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APPENDIX

Gene GALL, and Cecile Florence GALL,
Plaintiffs-Appellants,

v.

UNITED STATES of America,
Defendant-Appellee.

No. 75-2365

Summary Calendar.*

UNITED STATES COURT OF APPEALS,
Fifth Circuit.

Oct. 23, 1975.

Appeal from the United States District Court for the Northern District of Texas.

Before, GEWIN, GOLDBERG and DYER, Circuit Judges.

DYER, Circuit Judge:

This is an action for recovery of federal gift taxes previously paid by Gene Gall and his wife, Cecile Florence Gall. The only issue presented is whether certain gifts by the Galls to trusts for the benefit of their two children qualify for the annual gift tax exclusion provided by 26 U.S.C.A. Sec. 2503. The district court concluded that the gifts did not qualify for the exclusion. We agree and affirm.

*Rule 18, 5 Cir.; see Isbell Enterprises, Inc. v. Citizens Casualty Co. of New York et al., 5 Cir. 1970, 431 F.2d 409, Part I.

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On September 9, 1960, the Galls created two identical trusts, naming their daughter, Denise, beneficiary of one trust, and their daughter, Terry, beneficiary of the other. Under the relevant provisions of the trust instruments, the trustee was authorized to distribute to or apply for the benefit of the beneficiary so much of the trust income and principal as it in its sole discretion determined, until the beneficiary reached the age of twenty-one. At that time, the trusts were to terminate, and the trust property was to be distributed to the beneficiary.1/

The provisions of the trusts which cause concern relate to termination in the event of the beneficiary's death. If the beneficiary died before the trust otherwise terminated, the trust property would be distributed to whomever the beneficiary appointed by will; in default of appointment, the property would be distributed to the surviving issue of the settlors, or, in the absence of such issue, to the beneficiary's estate. The trust also provided that the power of appointment could not be exercised until the beneficiary reached the age of

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1/ The trust could be extended by written election of the beneficiary for an additional nine years. This election provision does not affect the present decision.

nineteen.2/ As will be seen, this was the trusts' fatal flaw.

26 U.S.C.A. Sec. 2503(b) provides that the first $3,000 of gifts made to

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2/ The trusts provided in pertinent part:

> Should [the beneficiary] die before attaining the age of twenty-one (21) years...this trust shall terminate, and the entire trust property then remaining shall be paid over and distributed to such persons in such shares, and in such manner as [the beneficiary] may appoint by her last will, duly admitted to probate by a Court of competent jurisdiction, provided this power of appointment is specifically referred to by the terms of such will; and provided, further, that this power of appointment can be exercised by [the beneficiary] only in the event that she is over the age of nineteen (19) years at the time of executing such will.
>
> Should the [beneficiary] die before attaining the age of twenty-one (21) years...and without validly exercising the general testamentary power of appointment [referred to above], the Trustee shall pay over and distribute the entire trust property then remaining to the then surviving issue of the Grantors in such equal shares per stirpes, or if there be no such issue of the Grantors then surviving, to the person or persons who shall be appointed to administer the estate of the beneficiary to be disposed of as a part of such estate.

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any person during any calendar year shall not be subject to the federal gift tax. This exclusion, however, is expressly inapplicable to gifts of future interests - they are taxable without regard to the $3,000 exclusion. The future interests limitation created substantial difficulty for donors seeking to make gifts in trust for minors; such gifts were generally deemed future interests, not qualifying for the exclusion. See, e.g., Commissioner v. Disston, 1945, 325 U.S. 442, 65 S.Ct. 1328, 89 L.Ed. 1720; Fondren v. Commissioner, 1945, 324 U.S. 18, 65 S.Ct. 499, 89 L.Ed. 668.

In response to this problem, Congress enacted 26 U.S.C.A. Sec. 2503(c), providing that certain gifts to minors would qualify for the exclusion, even though they might be future interests.3/ Under that provision, no part of a gift to a person under the age of twenty-one shall be considered a gift of a future interest if the property and income therefrom:

(1) may be expended by, or for the benefit of the donee before his attaining the age of 21 years, and

(2) will to the extent not so expended -

3/ S.Rep. No. 1622, 83rd Cong., 2d Sess. 478 (1954), 3 U.S. Code Cong. & Admin. News, p. 5123 (1954); H. Rep. No. 1337 83rd Cong., 2d Sess. - (1954), 3 U.S. Code Cong. & Admin. News, p.4465 (1954).

(A) pass to the donee on his attaining the age of 21 years, and

(B) in the event the donee dies before attaining the age of 21 years, be payable to the estate of the donee or as he may appoint under a general power of appointment as defined in section 2514(c).4/

All parties agree that the gifts in issue are gifts of future interests, and qualify for the annual exclusion only if the requirements of Sec. 2503(c) are met.

Under the terms of the trust, the property and income of the trust may be expended for the benefit of the beneficiary, and to the extent not so expended, will pass to the beneficiary when she reaches the age of twenty-one. Thus, the requirements of Sec. 2503(c)(1) and (c)(2)(A) are not in issue.

The trust provides that in the event of the beneficiary's death before reaching twenty-one, the corpus is payable first to the settlors' surviving issue in default of appointment by the beneficiary. Since the corpus is not payable to the estate of the beneficiary,

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4/ Section 2514(c) defines "general power of appointment" as a "power which is exercisable in favor of the individual possessing the power..., his estate, his creditors, or the creditors of his estate" subject to certain exceptions.

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the first portion of Sec. 2503(c)(2)(B) is inapplicable, and, according to the second portion of Sec. 2503(c)(2)(B), the annual exclusion will apply only if the beneficiary possesses a general power of appointment while under the age of twenty-one. The government argues that since the trust prohibits the beneficiary from exercising the power of appointment until she reaches the age of nineteen, the absolute requirement of Sec. 2503(c)(2)(B) is not met.

The unconditional wording of Sec. 2503(c) indicates that any restriction or limitation on the donee's ability to exercise the power of appointment would render that section ineffective. However, this interpretation has been rejected by the Commissioner in promulgating appropriate regulations. Recognizing that state law might limit the donee's ability to exercise the power, the regulation provides that if the minor is given a power of appointment exercisable during his lifetime or is given a power of appointment exercisable by will, the fact that under the local law the minor is under a disability to exercise the power does not cause the transfer to fail to satisfy the conditions of Sec. 2503(c). 26 C.F.R. Sec. 25.2503-4(b). This court has found reasonable restrictions imposed by state law to be nondisqualifying in other contexts under Sec. 2503(c), Ross v. U.S., 5 Cir. 1965, 348 F.2d 577, and we find this regulation to be reasonable in the present context. Were the law otherwise, state law in many instances would render it impossible to comply with Sec. 2503(c), and Congressional intent would be frustrated.

The Galls point to Texas law, which provides that a person may not execute a will, and therefore the testamentary power of appointment, until they have attained the age of nineteen. 17A V.A. T.S. Probate Code, Sec. 57 (1956). If this were the only controlling provision of Texas law, then the disability found in the trust, limiting the exercise of the power of appointment, would be created by local law, not by the terms of the trust. However, under the same provision of state law, all persons under the age of nineteen may execute a will if they are or have been married. Id.

The trust instrument only provides that the power cannot be exercised until the beneficiary reaches the age of nineteen. No exception is made in the event the beneficiary marries. Thus, a disability to exercise the power is created, not by local law, but solely by the terms of the trust. For example, if the beneficiary married when eighteen years old, she could validly exercise the power by will under Texas law, but would be prevented from doing so by the terms of the trust. Such disability is substantive within the meaning of the regulations[5/] and renders the savings provision

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5/ 26 C.F.R. Sec. 25.2503-4(b) provides that

> if the transfer is to qualify for the exclusion under this section, there must be no restrictions of substance (as distinguished from formal restrictions of the type described in paragraph (g)(4) of Sec. 25.2523(e)-(1) by the terms of the instrument of transfer on the exercise of the power by the donee.

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of Sec. 2503(c) ineffective. The gifts in question constitute gifts of future interests, and do not qualify for the gift tax exclusion.

Affirmed.

UNITED STATES COURT OF APPEALS

FIFTH CIRCUIT

No. 75-2365 - Gene Gall, and Cecile Florence Gall vs. U.S.A.

Dear Counsel:

This is to advise that an order has this day been entered denying the petition ( ) for rehearing, and no member of the panel nor Judge in regular active service on the Court having requested that the Court be polled on rehearing en banc (Rule 35, Federal Rules of Appellate Procedure; Local Fifth Circuit Rule 12) the petition ( ) for rehearing en banc has also been denied.

See Rule 41, Federal Rules of Appellate Procedure for issuance and stay of the mandate.

Very truly yours,

EDWARD W. WADSWORTH, Clerk

by /s/ Susan M. Gravois
Deputy Clerk

/smg

IN THE UNITED STATES DISTRICT COURT

FOR THE NORTHERN DISTRICT OF TEXAS

DALLAS DIVISION

GENE GALL AND WIFE, CECILE FLORENCE GALL	)	CIVIL ACTION
VS.	)	NO. 3-7072
UNITED STATES OF AMERICA	)	

J U D G M E N T

The above entitled action came on for non-jury trial before the Court, the Honorable Robert W. Porter, Judge, presiding and the issues having been duly tried and a decision having been duly rendered, the Court ORDERS that the Plaintiffs take nothing, that the action be dismissed on its merits, and that the Defendant United States of America recover of the Plaintiffs Gene Gall and Cecile Florece Gall its costs of action.

UNITED STATES DISTRICT JUDGE

April 7, 1975

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IN THE UNITED STATES DISTRICT COURT

FOR THE NORTHERN DISTRICT OF TEXAS

DALLAS DIVISION

GENE GALL AND WIFE, CECILE FLORENCE GALL	)	CIVIL ACTION
VS.	)	NO. 3-7072-F
UNITED STATES OF AMERICA	)	

MEMORANDUM OPINION

This is a suit by Gene Gall and his wife, Cecile Florence Gall, Plaintiffs, for the refund of $8,097.12 in federal gift taxes and interest for the years 1960 and 1962 through 1966. The sole question presented is whether the gifts by Plaintiffs to trusts for the benefit of their two children qualify for the donee annual exclusion provided by 26 U.S.C. Sec. 2503 (1972). The merits of this action came before the Court at a non-jury trial and this opinion is submitted in lieu of findings of fact and

conclusions of law.

There are two identical trusts in issue and each of the Gall children is a beneficiary of one of them. The relevant portions of the trust instruments are re-printed in an appendix to this opinion. Under the provisions of the trust instruments, the Gall children were not permitted to exercise a power of appointment by will over the trust property until they reached the age of nineteen. If the beneficiary of either trust died before reaching the age of twenty-one and the death was prior to an exercise of the power of appointment valid under the trust, the corpus of the trust did not go to the beneficiary's estate but instead was to be distributed among the surviving issue of the settlors of the trust. It is stipulated by the parties that neither of the beneficiaries reached the age of nineteen during the

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years involved in this litigation. Both are female.

Section 2503 provides a taxpayer an annual exclusion from gift tax liability of up to $3,000.00 for each gift. Generally, the exclusion is denied for gifts of future interests, but recognizing that it is customary for parents to delay control over gifts to minors until their majority, Congress in Section 2503 (c) provided that no part of a gift to a person under the age of twenty-one shall be considered as a gift of a future interest:

> "...if the property and income therefrom--
>
> (1) may be expended by, or for the benefit of, the donee before his attaining the age of 21 years, and
>
> (2) will to the extent no so expended--
>
> (A) pass to the donee on his attaining the age of 21 years, and

(B) in the event the donee dies before attaining the age of 21 years, be payable to the estate of the donee or as he may appoint under a general power of appointment...."

See S.Rep.No. 1622, 83rd Cong., 2d Sess. 478 (1954), 3 U.S.C. Cong. & Adm. News, p. 5123 (1954). The Secretary of the Treasury has promulgated the following regulation concerning this provision:

"Either a power of appointment exercisable by the donee by will or a power of appointment exercisable by the donee during his lifetime will satisfy the conditions set forth in paragraph (a)(3) of this section. However, if the transfer is to qualify for the exclusion under this section, there must be no restrictions of substance (as distinguished from formal restrictions of the type described in paragraph (g)(4) of Sec. 25.2523(e)-1) by the terms of the instrument of transfer on the exercise of the power by the donee. However, if the minor is given a power of appointment exercisable during lifetime or is given a power of appointment exercisable by will, the fact that under the local law a minor is under a disability to exercise an inter vivos power to fail to satisfy the conditions of section 2503(c) ..." 26 C.F.R. Sec. 25.2503-4(b)

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(emphasis added).

This interpretation has found support in the courts. Ross vs. United States, 348 F.2d 577 (5th Cir. 1965); Williams vs. U.S., 378 F.2d 693 (Ct. Cl. 1967).

It is the government's position that when relevant state law concerning the power by appointment by will is interposed, the Gall trusts do not meet the requirements of Section 2503(c)(2)(B). The contention is that although according to the cited regulation a disability on the exercise of the power created by local law does not cause the gift to fail to satisfy the statute, any restriction imposed by the trust instrument itself which is greater than those imposed by local law removes the transfer from the ambit of Section 2503(c). I agree. The plain meaning of the statute is that if the donee of a gift dies before reaching twenty-one years and the pro-

ceeds are not payable to her estate, then to qualify for the exclusion she must have been able to exercise a power of appointment while under the age of twenty-one. Logically, the regulation interprets the provision as not applicable if the donee is prohibited by state law from exercising the power. See Williams, supra. Thus, the Plaintiffs are not entitled to the exclusion if the trusts create a restriction on the exercise of the power of appointment by the donee that is more restricted than Texas law.

Provisions of the Texas Probate Code in effect at the time of the gifts in question gave to a female under the age of nineteen the right and power to make a will if that female was or had been married. V.A.T.S. Probate Code Sec. 57 (1956). Females over the age of fourteen could marry with parental consent.

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From age eighteen upward, females not under a legal disability had complete ability to enter into marriage without parental consent. Vernon's Ann.Civ.St. Arts. 4603, 4603(1960). The parties have stipulated that neither of the beneficiaries were under any disability that could have prevented a marriage.

Interposing these provisions upon the trusts in issue, it is clear that the instruments do not meet the requirements of Section 2503(c). It will be remembered that the trust instruments prohibited the property from going to the beneficiaries' respective estates and restricted them from disposing of the corpus by will until after reaching the age of nineteen. Since it was feasible under Texas law that the daughters could have legally married at the age of fourteen and thereby gained the right to exercise a power of appoint-

ment in a will, the trusts are more restrictive than state law. The gifts therefore remained future interests and did not qualify for the exclusion.

At trial the Plaintiffs introduced evidence that they had fully intended to meet the requirements of Section 2503 when they executed the trusts. A reading of the instruments certainly gives that impression, but it is also true that the former intentions of litigants are not controlling of tax consequences unless there is some ambiguity in need of explanation. See C.I.R. vs. Duberstain, 363 U.S. (1960); U.S. vs. Williams, 395 F.2d 508 (5th Cir. 1968); Cf. Harris vs. C.I.R., 461 F.2d 554 (5th Cir. 1972). The instruments in issue in this case, however, are iminently clear and unambiguous on their face, and I cannot now consider evidence of the Plaintiffs' original intent. As stated by the Fifth

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Circuit in U.S. vs. Hertwig, 398 F.2d 452, 455 (1968), "[t]he question is simply whether the parties have, or have not, set up a transaction which the tax law regards as [meeting the exclusion requirements]." Here they have not.

For the reasons stated, I find that judgment should be entered in favor of the Defendant.

It is so ORDERED.

UNITED STATES DISTRICT JUDGE

April 7th, 1975

In the Supreme Court of the United States

OCTOBER TERM, 1975

No. 75-1204

GENE GALL, ET UX., PETITIONERS

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

MEMORANDUM FOR THE UNITED STATES IN OPPOSITION

The question in this federal gift tax case is whether gifts made by petitioners to trusts established for the benefit of their two minor children were present interests so as to qualify for the annual gift tax exclusion provided by Section 2503 of the Internal Revenue Code of 1954 (26 U.S.C.). The decision below held that the gifts were future interests and did not qualify for the exclusion.

The pertinent facts are as follows: On September 9, 1960, petitioners created two identical trusts, naming their five-year old daughter beneficiary of one trust and their four-year old daughter beneficiary of the other trust. Under the terms of the trusts, the trustee (Republic National Bank of Dallas) was given discretionary authority to distribute income and principal to the beneficiary or to apply those funds for her benefit, until the beneficiary reached the age of 21. At that time, the trusts were to terminate and the corpus was to be

distributed to the beneficiary (Pet. App. 25). In the event the beneficiary died before reaching the age of 21, the trust property was to be distributed to whomever the beneficiary appointed in her will. However, each trust further provided that the power of appointment could not be exercised until the beneficiary reached the age of 19 and that if the beneficiary died without exercising her power, the trust property would pass to the petitioners' surviving issue (Pet. App. 25-26).

During the years 1960 through 1966, petitioners made various gifts to the trusts, and filed gift tax returns claiming the annual $3,000 gift tax exclusion provided for by Section 2503 of the 1954 Code. On audit, the Commissioner disallowed the annual exclusions claimed by petitioners on the ground that their gifts to the trusts were future interests. In this refund suit, the district court upheld the Commissioner's determination (Pet. App. 33-41), and the court of appeals affirmed (Pet. App. 24-31).

The decision below correctly held that petitioners' gifts were future interests and did not qualify for the annual gift tax exclusion. Petitioners' principal argument (Pet. 11-14) is that the gifts qualify as present interests under the special rule applicable to gifts to minors provided by Section 2503(c). But as both courts below correctly concluded, Section 2503(c) is inapplicable.

Under that provision a gift to a person under 21 years of age will not be considered a gift of a future interest in property if the property and the income therefrom may be expended for the benefit of the donee during his minority, and will, to the extent not so expended, pass to the donee upon his attaining the age of 21, and to his estate, or to whomever he might appoint under a general power of appointment, in the event the donee dies before attaining the age of 21.

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Here, the trust property was not payable to the estate of the beneficiaries in the event either of them died before reaching the age of 21 nor were the gifts subject to a general testamentary power of appointment exercisable by the benficiaries. Thus, the seond condition of Section 2503(c) was not met.[1]

While the trust instruments nominally granted each beneficiary a power of appointment, they expressly limited the exercise of those powers by providing that the beneficiary could not exercise her power until she was more than 19 years old. Pursuant to Section 25.2503-4(b) of the applicable Treasury Regulations on Gift Taxes (1954 Code) (26 C.F.R.), this limitation constituted a substantial restriction on the beneficiary's power of appointment so as to render the trusts ineligible for the Section 2503(c) exception. The regulation provides that if the exercise of the donee's power of appointment is subject to any substantial restriction by the terms of the instrument of transfer, Section 2503(c) is inapplicable unless the restrictions imposed by the donor are no greater than those imposed by the applicable state law.

As the decision below observed (Pet. App. 30), under Texas law, any married or previously married female may execute a valid will and thereby exercise a tes-

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[1] *Rollman* v. *United States*, 342 F.2d 62 (Ct. Cl.), *Gilmore* v. *Commissioner*, 213 F.2d 520 (C.A. 6), and *Kieckhefer* v. *Commissioner*, 189 F.2d 118 (C.A. 7), relied upon by petitioner (Pet. 13), do not conflict with the decision below. *Rollman* involved the question whether the assignment of rental income to a trust which otherwise met the requirements of Section 2503(c) was a gift of a present interest. *Gilmore* involved a question whether the trustee's powers to invade corpus was any greater than that provided by Maryland law. Finally, the issue in *Kieckhefer* was whether a power of invasion by a guardian who had not been appointed at the time of the trust prevented gifts to the trust from qualifying as present interests.

tamentary power of appointment, regardless of her age. 17A Probate Code, Vernon's Tex. Civ. Stat. Ann., §57 (1956).[2] Thus, petitioners' daughters could have married prior to reaching the age of 19 and thereby have acquired legal capacity to exercise a testamentary power of appointment. Under the trust provisions, however, they were precluded from exercising their powers of appointment until they were over that age, even if they married below that age. The trust provisions were thus more restrictive than the applicable Texas law,[3] and under the applicable regulation, petitioners' gifts do not qualify for the gift tax exclusion.

Contrary to petitioners' further contention (Pet. 11), Section 25.2503-4(b) of the Regulations does not impose a stricter test than the statute. Indeed, if anything, the regulation is more lenient than a literal reading of Section 2503(c) would require, since the terms of the statute would foreclose present interest treatment for all gifts to minors where there was any restriction—imposed by state law or otherwise—on the minor's exercise of his power of appointment.

It is respectfully submitted that the petition for a writ of certiorari should be denied.

ROBERT H. BORK,
Solicitor General.

APRIL 1976.

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[2]Moreover, females between the ages of 14 and 18 may marry with parental consent in Texas, and females 18 and over are free to marry without parental consent. 13 Vernon's Tex. Civ. Stat. Ann., Arts. 4603 and 4605 (1960).

[3]Petitioners' contention (Pet. 14) that the more lenient requirements of Texas law must be read into the trust provisions is without merit. A grantor of a trust can impose any conditions or restrictions he wishes on the beneficiary's enjoyment of the trust property, except those conditions that are illegal or violative of public policy. See 1 Scott on *Trusts* §4, p. 46 (3d ed., 1967). Obviously, the age restrictions imposed by the trust instruments here were neither illegal nor contrary to Texas public policy.

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